# United States Senate

WASHINGTON, DC 20510

July 21, 2004

The Honorable Donald E. Powell
Chairman
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429-9990

Dear Chairman Powell:

We are seeking your assistance to combat the growing problem of out-of-state banks partnering with in-state payday lending operations to bypass usury and consumer protection laws in states where this practice is restricted. It is our understanding that the FDIC has the authority to take enforcement action to end illegal bank-payday lender relationships. Many states have clearly banned the making of high interest rate, short term loans, but the FDIC's inaction to date is allowing this kind of exploitive lending to continue. We ask that the FDIC act consistently with other federal banking regulators and end illegal bank-payday lender partnerships immediately.

As you know, payday loans are extremely costly and their short terms make them difficult to repay, resulting in rollovers and consecutive transactions. The loans have triple-digit interest rates, often as high as 800% annual interest for a two-week loan. The high fees and short terms reduce the borrower's ability to repay the loan without a renewal, and payday lenders generate a disproportionate amount of fees from repeat borrowers.

The terms of these loans are so onerous that borrowers have difficulty making ends meet without taking out payday loans repeatedly, meaning that they often pay more in fees than they receive in principal. Many of our constituents have been trapped in a cycle of debt by payday loans. One group of concern has been members of the military and their families. The number of payday loan stores throughout the country has tripled since the late 1990s. These stores have proliferated around military bases, targeting young military families with limited financial resources. Studies have estimated that predatory payday lending is costing American families billions of dollars per year. The stories of trapped borrowers indicate that quantitative studies cannot capture the true financial and emotional toll on those families.

In states where laws regulate and restrict payday lending, payday lenders hide behind their bank partnerships with FDIC-regulated banks. The only reason for a payday lender to partner with a bank to make payday loans is to attempt to use the bank's right to export home state interest rates and to preempt state consumer protections that regulate payday lending. The payday lender markets the loans, solicits borrowers, accepts applications, disburses loan proceeds, services and collects the loans. The bank generally sells the majority of the participation of the loans – up to 95 percent – back to the payday lender on the same or next day. By allowing eleven state-chartered banks to "rent" their charters to payday lenders to get around usury laws and charge triple-digit interest rates, the FDIC is allowing federal preemption to harm consumers. We believe that this is a blatant abuse of bank powers, which threatens the integrity of the dual banking system by upsetting the balance between federal and state responsibilities.

No other federal regulatory body allows this activity. The Federal Reserve Board, the Office of the Comptroller of the Currency, and the Office of Thrift Supervision have all appropriately acted to shut down partnerships between the banks they regulate and payday lenders. The OCC and OTS have found that payday lending exposes federally-insured banks to unacceptable safety and soundness risks, undermines consumer protections, and carries serious reputational risks. By comparison, the FDIC has allowed the same payday lenders to operate with state-chartered banks. Sadly, the FDIC seems to have become the regulator of choice for payday lending companies who wish to misuse bank charters for the purpose of issuing payday loans in states with strict usury laws.

The FDIC's supervision of state-chartered banks is guided by the same regulatory framework that the other bank regulators used to end bank-payday partnerships. We encourage you to use the informal and formal supervisory actions available to you in a similar manner and shut down illegal bank-payday arrangements. Unlike the other federal banking regulators, the FDIC has failed to stop the bank-payday lender partnerships. The FDIC's acceptance of payday lending has resulted in more state-chartered banks entering into partnerships with payday lenders. In fact, the FDIC's tacit encouragement of banks engaged in payday lending is so strong that a bank formerly regulated by the Federal Reserve switched its charter to be regulated by the FDIC solely to allow it to continue its partnerships with payday lenders.

The FDIC should immediately end the practice of allowing payday lenders to abuse bank powers and undermine states' authority to uniformly regulate small loan companies and enforce usury laws. We would like to see the FDIC take action now to stop the partnerships between the banks you regulate and predatory payday lenders.

We ask that you submit to us a speedy response that outlines the steps you have taken or plan to take to enforce violations by FDIC member banks as it relates to illegal payday lending partnerships. We look forward to hearing from you on this very important matter.

Sincerely,

Senator Charles E. Schumer

Senator Paul Sarbanes

Senator Carl Levin

Senator Richard J. Durbin

Hillary Rodham Clinton

Senator Hillary Rodham Clinton

Senator John Corzine